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No. 2768

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

CRANE COMPANY, a Corporation,

Appellant,

vs.

FIDELITY TRUST COMPANY, Trustee, a Corporation, and WASHINGTON-OREGON ELECTRIC COMPANY, a Corporation, and WILLIS D. HOAG,

Appellees.

APPELLANT'S PETITION FOR REHEARING

Upon Appeal from the United States District Court for the Western District of Washington, Southern Division.

MAURICE W. SEITZ,
Solicitor for Appellant,

RANDOLPH W. CHILDS, MAURICE A. LANGHORNE, F. D. METZGER,
Solicitors for Appellee.

SCHWAB PRINTING COMPANY

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APPELLANT'S PETITION FOR REHEARING

Crane Company, intervener and appellant, respectfully petitions the court to grant a rehearing in this cause upon the following grounds:

First: The court in its majority opinion held that "the payment of interest to bondholders entitled to payment of interest in priority to the claims of creditors claiming is not a diversion." While I am somewhat in doubt as to what the court intended to

convey by this language, the import, when applied to the facts recited, is, that the payment of interest on bonded indebtedness to the exclusion of current indebtedness is not a diversion within the meaning of that term as defined in the adjudicated cases on the subject. I maintain that the court fell into an error in making this statement as it has been specifically held that the payment of interest on the bonded debt to the exclusion of current creditors constitutes a diversion. Supporting this are the following cases:

Burnham v. Bowen, 111 U. S. 776.

C. & A. Ry. Co. v. U. S. & Mexican Trust Co., 225 Fed. Rep. 941.

Clark v. Central Ry. & Banking Co., 66 Fed. Rep. 805.

Clyde v. Richmond & D. R. Ry. Co., 56 Fed. Rep. 541.

Central Trust Co. v. Power Co., 200 Fed. Rep. 89.

Southern Ry. Co. v. Carnegie Steel Co., 176 U. S. 285.

International Trust Co. v. Townsend Brick Co., 95 Fed. Rep. 850.

Furthermore in this case it is not necessary or essential to find a diversion in order to entitle the appellant to preference, as the stipulation entered into by the parties specifically eliminates that question by stating that if the appellant is otherwise entitled to preference, its claim should be allowed.

Transcript of Record, page 57.

Second: The opinion further recites that "Crane Company stands, we think, as a creditor which sold goods to the Washington-Oregon Corporation, with the expectation of realizing profits as in ordinary commercial transactions." This is in direct conflict with the stipulated facts. It was in substance stipulated between the parties that these goods were sold in the reliance that they would be paid for out of the current income, and for that reason Crane Company permitted the account to continue, thinking and believing that the current income was being so applied.

Transcript of Record, Paragraph IX, page 55.

It therefore seems to me that this point should have been accepted by the court as an established premise.

Thrd: The court further held that Crane Company showed "no special equity upon which they can rest their claims." This finding I submit, with all due deference to the court, is not warranted by the stipulated facts in the case or by the holdings of the federal courts on the subject.

In the case of *Union Trust Co. v. Morrison*, 125 U. S. 611, the court held Morrison's equity a strong one "by reason of the protection afforded the property and assets of the railroad company."

In *Clark v. Central Ry. & Banking Co.*, 66 Fed. Rep. 805, the court held the equities especially favorable to the intervenors because "it appears that there

was a diversion of the income *by the payment of interest on bonds* * * *."

In the case of *Central Trust Co. v. Colo. Light & Power Co.,* 200 Fed. Rep. 89, the court held that a diversion of the net income of the plant to the payment of interest or for permanent improvements *would create an equity in favor of unpaid claims of material men.*

In the case of *Gregg v. Metropolitan Trust Co.,* 197 U. S. 182, the court intimated that had a diversion occurred to the benefit of the secured creditors it would have constituted an equity in favor of the intervenor. To the same effect is the case of *Southern Ry. Co. v. Carnegie Steel Co.*, 176 U. S. 273.

I respectfully urge the court to review the above decisions with this point in mind, when it will be seen that what was held to be special equities in those cases are all consolidated in this case, viz: (1) A surplus net income out of which appellant's claim can be paid. (2) Diversion of current income to the payment of interest on bonded debt. (3) Materials furnished by Crane Company which inured to the benefit of the mortgage creditors and constituted a portion of the property which was sold under the foreclosure sale. (4) The goods furnished conserved the mortgaged estate and enhanced the value thereof.

Fourth: The holding of the court on the classification of the appellant's claims is not, I submit, in accordance with the stipulation of facts or the established doctrine.

In the parent case of *Fosdick v. Schall,* the supreme court's classification was for "necessary operating and managing expense, proper equipment and useful improvement." This has not been changed by any later holding of the supreme or federal courts, if you will take into consideration the facts of the particular case.

The case of *Gregg v. Metropolitan Trust Co., supra,* which the court cited as governing, states the same doctrine only in a different form. "To enable the railway company to operate as a continuing business."

In the case of *International Trust Co. v. Townsend Brick Co., supra,* the court defines it as "necessary operating and managing expense." This court in the case of *Moore v. Donahoo,* 217 Fed. Rep. 184, allowed claims for "operation and maintenance."

I submit that if the court will but consider the business of the company, namely, to furnish water, and the means by which this was accomplished, or could be accomplished, it will see the utter impossibility of continuing the business without the necessary equipment to connect its customers with the mains.

In addition to this there is a considerable portion of the claims presented which is stipulated to be for repairs, but the court apparently made no distinction. If a denial of appellant's claims are to be placed upon that ground, it should have the benefit of this distinction.

Fifth: The court in its majority opinion did not pass on the question as to whether the Washington law as laid down in the case of *Bellingham Bay Imp. Co. v. Fairhaven Ry. Co.,* 49 Pac. Rep. 514, should govern or whether it was pertinent. In view of the decisions cited on that question by Judge Gilbert, in his dissenting opinion, I maintain that we are entitled to the application of the law as laid down in the Washington case referred to, and to have that question passed upon.

Sixth: The court in its majority opinion, while holding that the appellant was not entitled to preference out of the *corpus of the estate* did not pass upon the question as to what appellant's rights were with respect to the *net income of the receivership.* The stipulation of facts shows that at the close of the receivership *there was a net income in the hands of the receiver amounting to $23,091.44.*

Transcript of Record, page 79.

In the case of *Gregg v. Metropolitan Trust Co., supra,* upon which the court seemed to place much reliance, an entirely different conclusion would have been reached had there been either a diversion or a surplus income in the hands of the receiver. Nay, more, the supreme court in that case held practically that the right of an intervenor under the circumstances here presented, to an allowance, out of the income of the receivership, is a conceded fact. To quote the exact language:

> *"It is agreed that the petitioner may have a claim against surplus earnings, if any, in the hands of the receiver, but that question, is not before us."*

The opinion of this court as expressed in *Moore v. Donahoo, supra,* is in full accord with this holding as indicated by the following language:

> "If, as is thus held, the *current income* constitutes a trust fund and if the mortgagee in taking his security impliedly agrees that labor and material men may first be paid out of the funds before he has any claim thereto, and if one performs labor or supplies materials *in reliance upon this understanding,* it follows as a matter of course that he has a right which a court of equity may assist him to enforce." * * *

The same reasoning and theory is adopted in the following cases:

Va. & Ala. Coal Co. v. Ry. Co., 170 U. S. 365.

Fosdick v. Schall, supra.

International Trust Co. v. Townsend Brick Co., supra.

Clark v. Richmond & D. R. Ry. Co., supra.

So. Ry. v. Carnegie Steel Co., supra.

I respectfully urge the court to examine the cases above cited with reference to this particular point, as I feel confident the court will find that an entirely different rule applies and should apply where there is a *net income* out of which claims may be paid and should have been paid. The theory underlying the

doctrine is that the mortgage creditors are, under no circumstances, entitled to anything out of the income until the current bills are paid, and if by any indirection or otherwise the secured creditors succeed in getting possession of these earnings to the exclusion of the creditors, restitution will be made in an appropriate proceeding.

For the foregoing reasons therefore I respectfully ask the court to grant a rehearing of this case, particularly upon the points suggested, and if the court deems it advisable, upon the whole case in order that ample justice may be done between the parties.

Respectfully submitted,

Maurice W. Seitz,
Solicitor for Appellant.

State of Oregon, County of Multnomah, ss.

I, Maurice W. Seitz, solicitor for the appellant, and petitioner, Crane Company, do hereby certify that I have read the opinion of this court in this case, dated December 4th, 1916, and the dissenting opinion of Judge Gilbert filed on said date; that I prepared the foregoing petition for rehearing.

I further certify that in my judgment said petition is well founded, and it is not interposed for delay.

MAURICE W. SEITZ,
Solicitor for Appellant.